Statement of

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I. Introduction

Chairman McCain, Senator Hollings, I am Terrell B. Jones, President and Chief Executive Officer of Travelocity.com, the leading online travel Web site. I appreciate the opportunity to appear before the Committee this morning to discuss the critical issues relating to travel distribution systems and the Internet.

Travelocity.com provides reservations capabilities for 95 percent of all airline seats sold, more than 47,000 hotels, more than 50 car rental companies and more than 5,000 vacation and cruise packages. This reservations capability is paired with access to a vast database of destination and interest information. To date, Travelocity.com has sold more than 6 million airline tickets and has more than 20 million members.

The online travel market in which Travelocity.com participates is growing at an incredible pace and, according to PhoCusWright, "is the fastest growing e-commerce category, poised to surpass $20.2 billion by 2001."[1] With the rise of the Internet, independent travel agents – both brick and mortar and virtual storefronts -- are increasingly seizing this nascent distribution channel to expand the richness and reach of their product and service offerings to the ultimate benefit of consumers. I believe the role played by such agents -- delivering rapid, comprehensive travel information to consumers -- is critical in maintaining and enhancing effective competition in the commercial airline transportation industry. As we are in the midst of what appears to be an era of airline consolidation -- through merger, via

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[1] PhoCusWright Online Travel Investor Report, p.1, Vol 2, Number 3, April 2000.

"alliances" in numerous forms, by hub consolidation and code-sharing agreements -- the role of independent consumer-centric agents - becomes even more essential.

A key component to continued growth and consumer gains in the Internet travel market is fair access to information from travel suppliers and, in particular, access to travel suppliers' lowest fares, corresponding inventory, and selling tools. We believe this issue of fair and open access to information is appropriate for this Committee to review, as it raises substantial commerce, transportation and consumer public policy questions. Again, I very much appreciate the Committee's attention to this issue and the opportunity to address the Committee with my testimony.

II. <u>Travelocity.com and the Online Travel Distribution Channel</u>

Travelocity.com is a true pioneer of Internet commerce. Since our initial launch in March 1996, our customer base has grown to more than 20 million members. We have built this successful business and a solid brand by constantly innovating and creating new products that take advantage of Internet technologies to bring benefits to consumers and travel suppliers alike. We truly believe we are changing the way consumers shop for and buy travel. Some of our new features and services include: (i) Alternate Airports – which provides alternative city fare information (often bypassing hub airports) in response to a given fare request;[2] (ii) "Dream Maps" – which offers leisure travelers on a limited budget the ability to view "theme" vacations (i.e., beach, ski or national park packages) that compare and

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2 *See* Ex. 1.

select among the best fares for multiple destinations,[3] and (iii) Best Fare Finder – a revolutionary product that shows consumers calendar-based fare offerings, so that they know precisely when advertised low fares are really offered. While travel suppliers are singularly focused – as they should be – on working to improve so-called "yield management" and maximizing the amount of revenue they receive with each sale of inventory, at Travelocity.com we are equally focused on providing *consumers* with what they want. We have invested heavily to improve the speed and functionality of our site so as to benefit our users. As noted by one airline industry analyst, "the philosophy [of independent travel web sites] is to push the price lower -- a complete reversal of the aims of an airline's own yield management team." [4]

Travelocity.com creates a global storefront for consumers to see, experience, research and buy their travel in one place. As such, Travelocity is the "front-end" or user interface through which consumers access a vast virtual warehouse of travel information, such as supplier inventory, prices and schedules. Just like any other travel agency in the world, Travelocity contracts with one of four computer reservation systems or CRSs for access to this supplier information. Travelocity's agreement for these "back engine" services is with Sabre. As this Committee is well aware, CRSs are closely regulated by the U.S. Department of Transportation (and also by DOT's counterparts in Canada and the European Union) and are required,

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3 *See* Ex. 2.

4 *Reuters Finance* (Feb. 23, 2000) at <www.biz.yahoo.com>.

among other things, to provide unaltered, unbiased airline information to travel agencies.

Currently, the CRS rules in the United States regarding so-called "screen bias" do not apply to the distribution of airline information directly to consumers via the Internet. However, because we believe our customers want neutral and unbiased airline information, Travelocity does not re-order the information we receive from Sabre. Thus the schedule, price, and availability displays you see in Travelocity comply with DOT's rules. Travelocity simply takes the so-called structured data streams and puts the identical information into a more consumer-friendly format for consumers (similar in some ways to taking the old DOS commands and changing those keystroke entries into graphical "point and click" icons to enable consumers to easily navigate the site and utilize the information.)[5]

We do, of course, accept advertising from suppliers as does every other retail web site (and, indeed, every media outlet) with which I am familiar. On our home page we frequently run banner ads for particular suppliers (such as airlines, hotel chains and car rental companies) promoting their services. In addition, in several origin-destination markets, we will display a banner ad in response to the consumer's request, featuring a particular carrier or service. An example of such an advertisement is attached to my testimony.[6] We think it is quite obvious to any

[5] An example of this is attached as Ex. 3. As you can see, the information on the "green screen" provided by the CRS to the brick and mortar travel agencies is unaltered from the information in Travelocity.

[6] See Ex. 4.

consumer, particularly any Internet user, that what is being displayed is an advertisement and not a display of flight options.

Independent online travel agents also operate in consumer-centric ways that encourage price discounting by suppliers and enhance market penetration by small and startup airlines. Independent travel sites, such as Travelocity.com, offer these carriers the ability to use our technology to enhance their marketing efforts. For example, we can provide our customers with e-mails containing special offers from the carriers. We have done so frequently and have received a very favorable response from our customers and supplier partners. Some of those partners include Air Tran, ATA, Hawaiian Airlines and National Airlines. Where other carriers have been willing to work with us, we have done promotions with them as well.

III. Suppliers' Collective Efforts to Enter the Online Travel Channel

As I will discuss in greater detail below, in the last part of 1999, there was an apparent shift in the individual strategy and focus of airline suppliers in the U.S. in distributing their products (seat inventory and fares) via the Internet. Previously, these carriers had competed quite vigorously with each other, and with us, through improvements in the offerings of their separate web sites. In November 1999, however, four of the five largest carriers in the U.S. – Continental, Delta, Northwest and United -- announced they had formed a jointly owned, Internet-based sales/marketing agency. In January 2000, apparently some twenty-four additional carriers joined the venture.[7] In April 2000, American Airlines announced that it had

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7 According to the press release at the time, the following carriers agreed to participate: Aeromexico, Air Canada, Air France, Air Jamaica, Air New Zealand, Alitalia, All Nippon Airways, Aloha, American Airlines, American Trans Air, Ansett Australia, Air Tran

joined the venture as an equity owner. The still yet to be launched Internet airline sales/marketing agency was originally dubbed "T2" and has just formally announced its name as "Orbitz."[8]

The apparent distinguishing element of T2/Orbitz is that it will have "unique" access to the low fares and corresponding inventory of the equity owning and non-equity owning participating carriers, and is billed as creating "one stop" shopping and "the only place to go" for consumers who want to save money on airline travel. It is unclear why the airline suppliers apparently shifted resources, investment dollars and development away from their individual sites to collectively focus on investing in and developing a joint Internet sales and marketing agency. As reported in PhoCusWright's Online Travel Investor Report in April 2000, one supplier said "the only thing worse than dealing with 33,000 travel agencies is dealing with two" [evidently referencing Internet successes Travelocity.com and Expedia.]

Travelocity.com welcomes competition. Time and again over the last four years we have faced new competitors and each time we have redoubled our efforts to innovate and bring greater value to our customers. Thus, if T2/Orbitz is simply another online travel site preparing to compete on the merits of its

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Holdings, Asiana, Austrian Airlines, British Midland, COPA Airlines, CSA Czech Airlines, Hawaiian Airlines, Iberia, KLM Royal Dutch Airlines, Korean Air, LTU Intl, Mexicana, Midwest Express, Midway Airlines, Sabena, Spirit, Swissair, Singapore Airlines, Vanguard Airlines, and Varig. "Two Dozen Airlines Join Web Site Led by Four U.S. Majors," *Aviation Daily* (Jan. 14, 2000). Among the carriers absent from the group are Alaska, America West, Southwest and TWA.

8 At least some industry analysts opined that "T2" stood for "Terminate Travelocity," a contention T2 spokespeople deny. *See* "Southwest Airline's Success With On-Line Bookings," *New York Times* (Mar. 1, 2000). Others have suggested that T2 is a reference to Arnold Schwarzenegger's movie about a killer robot. "If the commission cuts were Terminator 1 for many agents, this new airline-owned Web site will be Terminator 2 for those still barely hanging on." *See* "T2 Creators Dismiss Trade's Anticompetitive Fears," *Travel Weekly* (May 29, 2000).

products and services -- and on the same level playing field as Travelocity, Expedia, Trip.com, Biztravel.com, Lowestfares.com and many others, then that challenge should be encouraged. Competition will no doubt lead to continued product innovations and gains for consumers and smaller carriers. If, however, the business purpose and goal of this supplier owned sales agency is to improperly tilt the competitive playing field – by withholding certain fare and inventory information from competitors -- I believe that is an entirely different matter. If that is the case, and public statements from T2/Orbitz's founders appear to support that proposition, I believe T2/Orbitz raises significant policy issues within the oversight of this Committee. As noted by Chairman McCain, "[t]here are clear antitrust implications with the airlines…running one Web site…. If each airline wanted to run one, then that would be another matter, but I think it's a great danger that could lead to higher airfares for average passengers." [9]

IV. <u>T2/Orbitz: The Suppliers' Online Joint Sales/Marketing Agency</u>

As policy makers debate "fair access to fare and inventory information," it is important to understand just what T2/Orbitz *is* and what it *is not*. While much is unknown about the joint airline sales and marketing site, by focusing on certain key questions, I believe that this Committee will be in a much better position to evaluate the nature of this collective effort by suppliers to establish a position in the online travel channel.

[9] "Travel-Proposed Ticketing Service Draws Scrutiny," CNN.com (June 9, 2000).

A. **How/Why was T2/Orbitz Formed?**

Our experience was that suppliers were relatively slow to enter the Internet travel distribution channel. The first airline web sites did not add significant functionality until 1997 (which is considered relatively late in Internet terms), many months after Travelocity and other online travel agencies had introduced their services to consumers.[10] At some point, the suppliers began to pay much closer attention to this emerging channel of distribution and reportedly developed "fears" that absent decisive action by suppliers, "non-airline entities can use [Internet] technology to interpose themselves in [our] business."[11] As one IATA official noted, airlines were "less aggressive" than other industry participants to adopt the Internet, thus increasing the airlines fear of losing control over distribution.[12]

Apparently, the airlines' collective response to the new Internet distribution challenges posed by "non-airline entities" was the November 1999 announcement of the formation of a jointly owned Internet sales and marketing agency -- T2/Orbitz. Public statements by the founders of T2/Orbitz make it clear that the underlying purpose of the effort was to respond to the increasing popularity of agents like Travelocity.com and to such sites' growing role and consumer affiliation in the distribution of air travel information.

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10 Jupiter Online Travel Report at 9 (June 1999).

11 "*IATA Legal Symposium on eCommerce,"* (presentation by Michael Feldman, February 2000).

12 *Id.*

B. What obligations are placed on participating suppliers?

Evidence of how T2/Orbitz intends to operate in the online travel channel may be found in its non-equity "Airline Charter Associate Agreement." Based on a draft of this agreement I have seen, airline participants may no longer have unique sales or run special promotions with online competitors of T2/Orbitz. Rather, participating carriers must give T2/Orbitz access to *all* "published fares," which, under the agreement, is broadly defined and includes virtually every fare in a given airline's inventory. This includes: (1) any fares published in a CRS (2) any fares, and corresponding inventory, published in the carrier's internal reservation system, (3) "Internet" fares, including those offered via e-mail to targeted consumers; (4) promotional fares offered to the general public; and (5) fares offered to travel consolidators.

In addition, the Agreement provides strong incentives for participating carriers to provide their lowest fares -- a major if not the major attraction for consumers -- exclusively to T2/Orbitz. Each participating carrier is obligated to provide T2/Orbitz with substantial "In-Kind Promotions" which can run into millions of dollars[13] for the first 12 months of the agreement. Among other things, "In-Kind Promotion" obligations can be satisfied by offering "exclusive promotions or fares available only on" T2/Orbitz or the participating airline's own Internet travel site.[14] T2/Orbitz also

[13] The exact total is calculated by the carrier's "Market Share multiplied by ___ million U.S. dollars".

[14] The value of these exclusive fares is calculated by the difference between the exclusive fare and the next-highest fare offered elsewhere, times the number of tickets. If the fare is made available on T2/Orbitz and not on the offering carrier's own web site, a 100% credit is applied toward the in-kind requirements; if the carrier determines to offer the fare independently, the credit is lowered to 75%. The "value" as calculated under this formula is capped up to $1 million dollars for any 12-month time period.

has the right to mutually develop the exact terms of the In-Kind Promotional plan and to determine how such obligations will be satisfied by the smaller carriers, and can withhold certain rebates if the carrier and T2/Orbitz fail to develop a mutually acceptable promotional plan and/or if the carrier fails to adhere to the terms of that plan.[15]

Moreover, T2/Orbitz's requirement that all participants immediately provide to T2/Orbitz all promotions and fares that are offered using alternative distribution methods will insure that T2/Orbitz lacks any incentive to innovate to attract special promotions from suppliers. As the Department of Justice has recognized in somewhat analogous circumstances, such a requirement will insulate T2/Orbitz from any competitive pressure because a participating carrier cannot force T2/Orbitz to improve its services by threatening to take its promotional offerings elsewhere. DOJ successfully urged DOT to remove such "most favored nations" provisions or "parity provisions" – clauses that require carriers to participate in all CRSs at the same level -- for carriers that do not own interests in CRSs.[16] In so urging, the DOJ noted that such a provision "removes an airline's ability to obtain better service by credibly threatening to downgrade its participation level. With the most favored nations or parity provision, the downgrade threat is unrealistic because the CRS knows that the airline would also have to lower its participation level in every other CRS."[17] As with the parity provisions at issue in that matter, participating carriers in T2/Orbitz cannot

15 The non-equity owning carriers can also apparently satisfy these requirements by providing T2/Orbitz with "passenger database information" and "competitive purchaser names" (e.g. e-mail addresses of passengers who booked travel through another online agency).

16 Comments of Department of Justice, Docket OST-96-1145 (Sept. 19, 1996).

17 *Id.* at 7.

simply divert their promotional efforts to other, more responsive, Internet travel sites without similarly offering those promotions to T2/Orbitz. T2/Orbitz's requirement that any fares and seats offered to other outlets also be offered to T2/Orbitz, will, under DOJ's and DOT's prior reasoning, render T2/Orbitz "unresponsive to consumer preferences" and "anticompetitive."[18]

We think it would raise serious public policy questions if major suppliers use their collective control over inventory and pricing information (and their ability to deny such information to competitors) to tilt the playing field in favor of their joint sales agency and against sites more aligned with consumer interests, such as Travelocity.com.[19] At least in the early stages after T2/Orbitz's announcement, some industry analysts appeared to endorse the joint supplier site: "Due to its size and backing, T2 will eventually take its place among the top three travel sites for both traffic and sales." [20] But, as an Internet industry publication recently noted,

18 *Id.* at 8 (citing *NCAA v. Board of Regents,* 468 U.S. 85 (1984)).

19 Although I am not a lawyer, this situation seems strikingly similar to a supplier joint venture formed by the major movie picture studios to "compete" against the then new premium pay-TV channel – Home Box Office. As I understand it, the major studios essentially agree to create a competitor to HBO (called Premiere) that would have exclusive access to certain of the studios' major releases for a certain time period – while such access would be denied to the increasingly popular HBO. *United States v. Columbia Pictures Indus., Inc.*, 507 F. Supp. 412 (S.D.N.Y. 1980). In rejecting the movie studios contention that this restriction was needed to "differentiate" their new service, the Court quickly noted that there were "a number of ways of achieving product differentiation without cornering the market" on Hollywood "hit" movies. *Id.*, 507 F. Supp. at 425. This appears entirely consistent with what the founders of T2/Orbitz have publicly stated -- that the formation of T2/Orbitz is "one of the strategies that the airlines have used in response" to the "danger" of electronic travel agents "completely dominating this space, to the detriment of the travel providers themselves."

20 "Top Airlines' New Travel Site Will Succeed," *The Forrester Brief* (Jan. 24, 2000).

"[w]hen the world's oldest and largest corporations announce they are cooperating to confront the future, the rest of the business world should be suspicious."[21]

C. **Assuming T2/Orbitz does not plan to withhold low fares and inventory from competing online travel sites, what is unique about this site?**

It would be difficult to expect that T2/Orbitz will have the same competition-enhancing features as those that will, and have been, developed by independent sites. As Alex Zoghlin, T2/Orbitz's Chief Technology Officer pointed out: "Not every airline is interested in full and complete disclosure to the consumer." [22] Industry analysts have noted as much: "The weak link in T2, analysts agreed, is that airlines would have to bring potential customers to a site where they could compare the fares of the different airline rivals—hardly a wise marketing strategy."[23]

The creation of a joint sales agency through T2/Orbitz does not offer a new technological breakthrough or create some new efficiency in the distribution of supplier inventory, fares or schedules to consumers. For many years such information has been available to travel agents and consumers via automated means, through computerized-reservation systems which collect and disseminate low fares for nearly all airlines. Moreover, airline-sponsored web sites are hardly uniquedis8-27.kor many yvi coopect ai toacon s MoEa co the dicarris viwhoor nm purcs b, whd dime booking capabilities.[24] All of this essentially begs the question of just what is T2/Orbitz.

D. **What lessons can be applied from the history of travel distribution to better evaluate this collective supplier effort?**

Our best guide to determining what T2/Orbitz is may be history. In the 1960's and 1970's, the airline industry developed the first networked industry infrastructure for electronic commerce—the computerized reservation system or "CRS". Interestingly, there was an initial joint supplier effort to create a single CRS from 1974 to 1976. While that effort ultimately failed, it is important to note that the airline suppliers sought the formal approval of the federal government (through a grant of antitrust immunity) *before* they engaged in those discussions and the DOJ, while granting approval, did so subject to a number of conditions. It is my understanding that in regard to T2/Orbitz – which the suppliers have indicated is their attempt to create essentially a new distribution channel to bypass all CRSs -- the suppliers have not sought pre-approval (though they say they have informally briefed Justice Department officials prior to issuance of subpoenas). Individual airlines or groups of airlines ultimately established carrier-affiliated CRSs -- and not unexpectedly -- the owning airlines utilized the best displays in their affiliated system to sell their inventory of airline seats. This Committee is familiar with the ensuing debate and study that occurred in the industry in the early 1980's that led to clear regulations in the distribution of airline information in the United States. These rules continue

24 As described above, several carriers have established web sites that offer virtually a full slate of competing fares offered by other major carriers. In addition, virtually all carriers maintain interlining agreements with other carriers that allow the airlines to sell connecting flights offered by competing carriers. Through these agreements therefore, virtually all major carriers are authorized to sell tickets of competing carriers.

to exist today, and have even been exported to Canada and the European Union, where they were expanded to cover the distribution of airline information directly to consumers.

In circumstances roughly analogous to that presented by T2/Orbitz, in 1992, the DOT adopted rules requiring "mandatory participation" by airline owners of CRSs in competing systems, partly at the behest of the DOJ (the DOJ supported that proposition in the original rule-making in 1984.) Essentially, DOJ and others were concerned that suppliers were withholding information and desirable consumer amenities, such as pre-reserved seats, boarding passes, etc. from competing CRSs – providing those items only through their affiliated CRS. As you might expect, it was believed that this conduct substantially undermined the utility and value of the competing CRSs. To ensure fair access to such information, the DOT required an airline supplier that owned a portion of a CRS to post the same information in competing CRSs that is posted in the carrier-owner's CRS.

DOT noted that many industry participants were alleging that carrier-owners had "reduced the level of their participation in other [CRS] systems in order to handicap the ability of other systems to compete for subscribers."[25] In requiring that owner-carriers participate in CRSs on equal terms, DOT noted that "[t]his requirement appears justified on competitive grounds, since it would prevent a CRS owner from using its dominance of a regional airline market as a

[25] DOT Notice of Proposed Rulemaking, 56 *Federal Register* 12586 (Mar. 26, 1991).

tool for obtaining dominance in the area's CRS market."[26] The rise of the Internet and the ability of travel suppliers to distribute products directly to consumers arguably creates similar concerns.

E. **<u>What is T2/Orbitz's Business Model and does it reveal anything about the joint supplier site's underlying purpose</u>?**

While we do not have access to all of the e-mails, agreements, or other documents that might conclusively demonstrate the business plan and actual intent, the business model set out by their primary consultant raises a number of issues. As set forth in *Blown to Bits*, recently published by Boston Consulting Group, the operator of T2/Orbitz under contract with the founding suppliers, BCG openly embraces and counsels conduct that appears to raise serious issues for those BCG clients that might choose to follow this advice.

In essence, BCG warns that independent Internet sites like Yahoo! And Travelocity.com have "tilted" the balance of power from sellers towards buyers. BCG outlines various features, such as unbiased comparison features and identification of alternative sources of supply, which they describe as the "consumer's gain" and the "seller's loss." In describing how incumbents "have a lot to lose" by the growth of consumer-affiliated (*i.e.*, independent) Internet sites, BCG suggests that product suppliers and traditional retailers "alike fear the rise of the agent navigator who facilitates broad-reaching comparisons without even being party to the transaction."

In order to counter that threat, BCG suggests that independent sites must be "denied critical mass"—or, in the words of the authors, "[i]f enough suppliers refuse

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[26] *Id.*

to sell through the e-retailer, or enough retailers refuse to provide information to the dispassionate agent, neither the e-retailer nor the agent can achieve critical mass."[27] Of course, BCG implicitly recognizes that achieving such concerted agreement is difficult in the absence of an agreement among competitors to boycott independent sites:

> Obviously, the seller can ultimately stop this game, if only by refusing to operate a Web site. But herein lies the second and more fundamental issue: *it is not obvious that it is in any one seller's interests to do so.* The most rigorously customer-affiliated navigator with the broadest reach is still a source of incremental business to a seller…. Therefore, while it is undoubtedly in the interests of all sellers *collectively*, it is not in the interest of any one seller individually to deny its own data to the navigator. But if everyone reasons that way, the navigator will achieve critical mass.[28]

In order to overcome this difficulty, BCG suggests that suppliers can stunt independent sites by "emulating the way the insurgent defines his business."[29] At the heart of this strategy are horizontal agreements among competitors. In this regard, BCG urges suppliers to create their own supplier-initiated sites that will, in essence, mislead consumers and disadvantage non-competing suppliers. Such supplier-initiated sites can "succeed," according to BCG, by using their sites to:

> "provide comprehensive but not necessarily comparable data on one's own products and those of direct competitors, and slightly bias the presentation through the ordering of alternatives and the occasional emphasis or omission."[30]

If T2/Orbitz is indeed predicated on its consultant's model, consumers will be the primary losers.

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[27] *Blown to Bits* at p. 115.

[28] *Id.* at 139-140 (emphasis in original).

[29] *Id.* at 119.

V. Conclusion

The rise of Internet commerce has initiated a true revolution in the travel distribution industry, and holds the promise of greater efficiency and enhanced competition at all levels. As a policy matter, and perhaps as a legal matter, I do not think suppliers should be able to engage in collective action to withhold information from so-called neutral navigators. Notwithstanding the limited information available about T2/Orbitz, based on industry information and T2/Orbitz's public statements, further investigation into this joint supplier sales and marketing site is warranted.

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[30] *Id.* at 142.